

1. Investigations of Criminal Offenses and Filing of Complaints

1) Outline

1. Authority to investigate criminal offenses

The authority to investigate criminal offences on securities transactions is given to the SESC under the Securities and Exchange Law (SEL), the Law on Foreign Securities Firms (LFSF) and the Financial Futures Trading Law (FFTL). The SESC's scope of investigations under that authority is not limited to securities companies, but reaches all parties involved in securities transactions, including the investors themselves. With the SEL being applied similarly, the SESC is also given the authority to investigate criminal offences under the Personal Identity Verification Law (PIVL).

Noncompulsory investigations conducted by the SESC on criminal offenses include making inquiries about suspects of criminal acts or related parties (hereinafter referred to jointly as "suspects"), inspection of materials in the possession of or left behind by suspects, and confiscation of materials supplied by suspects on a voluntary basis or left behind by them (Article 210 of the SEL, Article 53 of the LFSF, Article 106 of the FFTL and Article 18 of the PIVL). Compulsory investigations conducted by the SESC with warrants from judges include visiting and searching the premises of suspects and seizing related evidences (Article 211 of the SEL, Article 53 of the LFSF, Article 107 of the FFTL and Article 18 of the PIVL).

2. Scope of criminal offenses and others

Criminal offenses are defined as hampering fair securities trading, and their scope is prescribed under cabinet orders (Article 45 of the SEL Enforcement Order, Article 23 of the LFSF Enforcement Order and Article 14 of the FFTL Enforcement Order). Main offences include securities companies providing benefits to select clients to compensate for trading losses, issuing companies submitting securities statements and reports containing false information, insider trading, the spreading of rumors and the manipulation of prices.

Criminal offenses subject to investigations under the PIVL include customer acts of covering up their real names and addresses when the securities company verifies their identity.

SESC investigators report the results of criminal investigations to the SESC (Article 223 of the SEL, Article 53 of the LFSF, Article 119 of the FFTL and Article 18 of the PIVL). When convinced of a suspect's guilt, the SESC files a complaint with the public prosecutors and sends the evidence it gathered in its probe, including materials left behind by the suspect and seized materials (Article 226 of the SEL, Article 53 of the LFSF, Article 122 of the FFTL and Article 18 of the PIVL).

2) Filing of complaints

In the 2004 SESC year, the SESC conducted compulsory search of the homes and related offices of the suspects and necessary non-compulsory investigations in connection with the suspected criminal offenses.

Based on the results of investigations of the criminal offenses, the SESC filed a total of 11 complaints involving 18 individuals with the public prosecutors on charges of violation of the Securities and Exchange Law. These complaints consisted of 6 cases involving 10 individuals on charges of insider trading, 1 case involving 2 individuals on charges of spreading rumors and use of fraudulent means, 2 cases involving 2 individuals on charges of market manipulation, and 2 cases involving 4 individuals on charges of filing financial statement reports containing false information. The outline of these filed complaints is provided as follows:

(1) Media Lynks Corp. Case (1: Insider Trading)

As the differences arose between the expected figures projected in February and May 2003 in terms of net profit and dividends of Media Lynks Corp. for the fiscal year ended March 2003, the president of Media Lynks Corporation sold the shares of the company prior to the release of the latest projection as of May 2003 in an attempt to avoid a loss.

(2) Media Lynks Corp. Case (2: Dissemination of Rumors and Use of Fraudulent Means)

With the intent to make the stock price of Media Lynks Corp. soar, the company's president released the false information, stating that the total issue amount of the convertible bond that the company decided to issue on the Osaka Stock Exchange was paid in by the payment date when in fact the payment had not been made. Furthermore, he circulated the rumors and employed fraudulent means by announcing on the company's website that the conversion to stock of the bond had been completed partially and its capital was increased when in fact there were no assets added as the result of the bond issue as well as there were no assets to be applied to increase the capital in the event the warrants of the bond were exercised.

(3) Case Involving Stocks of Magara Construction and the Two Additional Stocks (Price Manipulation)

Intending to drive up the bid quotations and prices of stocks of Magara Construction Co., Ltd., Yamatane Corp. and Iwatsu Electric Co., Ltd. and induce active trading among these stocks, the suspect issued numerous buying orders in massive quantities from his home in the city of Kushiro, Hokkaido, through a number of securities companies over the Internet, using his own name at prices that ranged between 1 yen and 4 yen below the best bid in spite of the fact that he had no intention of actually buying these stocks. The suspect generated an appearance of vast buying orders, induced buying orders at high prices, drove up the stock prices, misled investors into believing that the stocks were actively traded, and also arranged to have a series of selling and buying orders executed to cause the price of each of these stocks to change.

(4) Media Lynks Corp. Case (3: Submission of a Financial Statement Report Containing False Information)

The president of Media Lynks Corp. submitted the financial statement reports containing the company's income statement and balance sheet that presented the false information for the fiscal year ended March 2003 in the course of the business operation of the company. That falsification was accomplished by such means of reporting of fictitious sales and purchases.

(5) CSK Communications Corp. Case (Insider Trading)

The executives and other employees of CSK Venture Capital Co., Ltd., which had been hired by CSK Communications Corp. to provide services in connection with the stock exchange listing of the CSK Communications Corp. stock, gained knowledge of CSK Communications Corp.'s decision to become a fully-owned subsidiary of CSK Corp. by exchange the stocks, and purchased the company's shares before the announcement of the plan.

(6) Chinon Industries Inc. Case (Insider Trading)

The suspect, who was an employee of the Ministry of Economy, Trade and Industry,

was engaged in the administration of reviews and approvals relating to corporate restructuring plans that were covered by the Special Measures Law Concerning Industrial Revitalization. He gained knowledge of the decision by Kodak Japan Digital Product Development Corp. to make a takeover bid of Chinon Industries based on the assumption Chinon would receive the application of the law, and bought shares of Chinon prior to the announcement of the decision in an attempt to gain profit.

(7) Nanno Construction Co., Ltd. Case (Insider Trading)

The executive officer of Nanno Construction Co., Ltd., who was also concurrently the director of the Kansai Division and the manager of the Wakayama branch of the company, and other individuals gained knowledge of the decision by the company to issue new shares by way of third party allotments and bought the company's shares with the intent to gain profit from the purchase of the company's shares before the decision was announced.

(8) Seibu Railway Co., Ltd. Case (1: Submission of Financial Statement Reports Containing False Information)

The Chairman of Kokudo Co., Ltd., in conspiracy with the President of Seibu Railway Co., Ltd., submitted the financial statement reports containing false information with respect to the certain material facts, including misrepresentation about Kokudo's ownership percentage of the total outstanding shares of Seibu Railway, which was approximately 43% when in fact it was approximately 65%.

(9) Seibu Railway Co., Ltd. Case (2: Insider Trading)

In the course of performing his job duties, the chairman of Kokudo Co., Ltd. learned of the fact that false information had been presented continually in Seibu Railway's financial statement reports regarding the major shareholder information of Seibu Railway that Kokudo owned, and sold shares that Kokudo owned to other companies in the course of the company's business operation in conspiracy with some Kokudo's employees and others in an attempt to reduce the number of shares owned by selling off part of the holdings prior to the announcement of the fact.

(10) Canon Software Inc. Case (Insider Trading)

The employee of a corporation that had been hired by Canon Software Inc. to provide services relating to legal advertising of a stock split of Canon Software Inc. gained knowledge of the decision by Canon Software Inc. to split its stock. He then purchased the company's shares with intent to gain profit by buying the company's shares before the decision was announced.

(11) Nissin Kogyo Co., Ltd. Case (Price Manipulation)

Between the second half of July 2001 and the first half of August of the same year and in connection with shares of Nissin Kogyo Co., Ltd., which was listed on the Second Section of the Tokyo Stock Exchange, the suspect committed the following acts.

a) In an attempt to boost the price of Nissin Kogyo stock and induce active trading in the stock, the suspect, using his own name and through multiple securities companies, manipulated the price of Nissin Kogyo stock by:

- Purchasing approximately 200,000 shares of the stock by such means as placing successive price limit buy orders to drive up the price while at the same time,
- Selling off approximately 160,000 shares of the stock and holding up the lows by

placing massive buy orders at lower levels. By employing these means, the suspect ordered the purchase of approximately 50,000 shares, making the stock price to surge.

b) With the aim of misleading others to believe that the stock was being traded actively, the suspect bought a total of approximately 100,000 shares of the stock in his own name and sold the same volume of shares at about the same time in separate transactions over the same period of time. These sales and purchases were sham transactions that were not intended for the actual transfer of ownership.

2. Administrative Civil Money Penalty Investigations

1) Purpose of and Authority for Investigations

The administrative civil money penalty system was introduced on April 1, 2005 to achieve administrative goals of curbing such acts of violations as insider trading and ensuring the effectiveness of regulations. It is an administrative measure that imposes monetary burdens on violators of certain provisions of the Securities and Exchange Law.

The Surveillance Commission is granted authority under the Securities and Exchange Law by the Prime Minister and the Commissioner of the Financial Services Agency to conduct investigations of suspects and other involved persons for the purpose of penalty investigation.

The authority for conducting penalty investigations (which do not extend to submissions of financial statement reports containing false statement) is set forth in Article 177 of the Securities and Exchange Law, which grants the Commission the power to

- (1) Question suspects or persons of interest, or demand opinions or reports from such individuals, and
- (2) Enter business offices of suspects and other sites that are necessary for investigation, and inspect accounting documents and other items.

The authority to conduct penalty investigations pertaining to submission of registration statements etc. containing false statement is set forth in Article 26 of the Securities and Exchange Law, which grants the Commission the power to take the following actions when deemed necessary and appropriate for the sake of public interest or investor protection:

- (1) To order a person who filed a registration statement, a person who filed a shelf registration document, a person who filed a financial statement report, a person who filed a report of treasury share purchase, an underwriter of securities or any other involved party to submit reports or data that are helpful for investigations, and
- (2) To inspect accounting records and other items of the individuals being investigated.

2) Acts Subject to Penalties

Specific acts that are subject to levying of penalties are as follows:

- (1) Submission of a registration statement etc. containing false statement (disclosures relating to subscriptions and sales) (Article 172 of the SEL)
- (2) Dissemination of rumors and use of fraudulent means (Article 173 of the SEL)
- (3) Price manipulation (Article 174 of the SEL)
- (4) Insider trading (Article 175 of the SEL)

Note: Submission of a financial statement report containing false information, etc. on or after December 1, 2005 will be subject to orders for payment of penalties.